



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Number: **201624023**
Release Date: 6/10/2016

UIL: 501.33-00

Date:
March 16, 2016
Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

Dear _____ :

This letter is our final determination that you don't qualify for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code (the Code). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

Because you don't qualify as a tax-exempt organization under Section 501(c)(3) of the Code, donors can't deduct contributions to you under Section 170 of the Code. You must file federal income tax returns for the tax years listed at the top of this letter using the required form (also listed at the top of this letter) within 30 days of this letter unless you request an extension of time to file.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection (as required under Section 6110 of the Code) after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Notice 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

We'll also notify the appropriate state officials of our determination by sending them a copy of this final letter and the proposed determination letter (under Section 6104(c) of the Code). You should contact your state officials if you have questions about how this determination will affect your state responsibilities and requirements.

If you have questions about this letter, you can contact the person listed at the top of this letter. If you have questions about your federal income tax status and responsibilities, call our customer service number at 1-800-829-1040 (TTY 1-800-829-4933 for deaf or hard of hearing) or customer service for businesses at 1-800-829-4933.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosures:

Notice 437

Redacted Letter 4036, *Proposed Adverse Determination Under IRC Section 501(c)(3)*

Redacted Letter 4038, *Final Adverse Determination Under IRC Section 501(c)(3) - No Protest*



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Date:
January 21, 2016
Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

UIL:
501.33-00

Legend:

P = business 1
Q = business 2
R = individual
S = individual
T = individual
X = state
y = date

Dear :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(3) of the Code. This letter explains the basis for our conclusion. Please keep it for your records.

Issues

Do you qualify for exemption under Section 501(c)(3) of the Code? No, for the reasons stated below.

Facts

You were incorporated in X on y. Your Articles of Incorporation state the specific purposes for which you are organized include, but are not limited to: the preservation and management of parkland and delivery of programs for scientific, historic, educational, ecological, recreational, agricultural, scenic or open space opportunities. It further states you are organized and operated exclusively for charitable purposes within the meaning of Section 501(c)(2) of the Code. You submitted an attestation that you amended your purpose clause to meet the requirements of Section 501(c)(3), but we have no evidence that an amendment was filed.

Your Bylaws state you are formed exclusively for assisting low income families to buy houses at affordable prices. Your Bylaws further state that not more than 25% of the persons serving on the Board of Directors at any time may be interested persons. An interested person is (1) any person currently being compensated by the Corporation/Organization for services rendered to it within the previous twelve months, whether as a full-time or part-time employee, independent contractor, or otherwise, excluding any reasonable compensation paid to a

director; and (2) any brother, sister, parent, ancestor; descendent, spouse, brother-in-law, sister-in-law, son-in-law, mother-in-law, or father-in-law of any such person.

You have two directors, one officer, and one employee. Two of your governing body members (R and S) are partners/owners of Q, a construction company. One of your governing body members (R) is the owner of P, a real estate brokerage limited liability company. P and Q will both perform paid services for you.

Your address is listed as "in care of P". P is also listed as your registered agent. Your Articles of Organization confirm that your mailing address, and principal office, is the same as that of P. One cover sheet faxed to our office in response to information requests contained the header and logo of P.

You describe the duties, and hours worked, of three of your board members. R listed his qualification for serving on your board as 'real estate broker', serving 10 hours weekly listing and selling properties. S, listed qualification as bookkeeper, 10 hours weekly, for accounting and bookkeeping. T, listed qualification as construction manager, 15 hours weekly, managing projects and construction. You describe the fourth member of your board as an employee performing office manager duties.

You plan to look into neighborhoods with abandoned properties to buy and fix houses, then resell them to low income families. This would revitalize high-poverty communities across the state by attracting investment, improving affordable housing, and expanding home ownership opportunities to help reduce violence. The renovated homes will be sold only to low income families. Your charitable project is to ensure you only sell renovated homes to low income families based on their income at very affordable prices. You help low income families who would not have qualified to buy their own houses realize the American dream of home ownership. You will provide single family housing for low income families, which will range from one to four bedrooms.

You also stated that you sell renovated single family properties and that all facilities are single units which will be sold to low income families. Residents buy the units from you. To date you haven't acquired any property. You plan to develop the land yourself or buy properties and renovate to sell.

You use the annual federal government guidelines designation for income levels to decide who qualifies as low income families. You use a first come first serve approach. You sell houses at very low prices to low income families in designated areas using the federal government poverty guidelines. You use income levels for each neighborhood and homeowners earn no more than 120% of the very low income levels for the area. You have restrictions on the maximum income levels that are allowed to buy your houses based on the neighborhoods and published poverty levels.

You do not participate in any government housing programs and you have no governmental supervision. You have not received an official designation as blighted for the area(s) in which your properties will be located. You make the public aware of your housing through workshops and flyers which will be distributed at designated zones.

No copies of flyers that you distribute, or materials related to workshops you conduct, were submitted with your application for exemption. Additionally, no details were provided regarding these workshops. When asked to describe your educational programs you responded with a one page budget plan for household spending and a one page housing priorities checklist. The only additional documents you submitted were a standard uniform residential loan application (URLA), the only application you require of potential homeowners, and a sample agreement for real estate purchase.

Your criteria to determine whether an applicant is low income were given as follows:

- Must have a gross income of at least \$25,000 per year but no more than \$40,000 per year
- Must be a United States citizen or permanent resident
- Must provide a two-year history of stable income and employment
- Must be willing to attend required workshops for homeownership
- Must have the ability to afford anticipated monthly payments, and
- Must have an acceptable credit history, which includes a good record of paying rent and utilities.

You then stated eligibility will be determined through the following:

- Applicant must be a U.S. citizen or a lawful permanent resident
- Applicant must not [sic] owned a home in the past 3 years or had a foreclosure in 7 years
- Applicant must currently live in an inadequate or unsafe home; and/or overcrowded home; and/or a physically unsafe neighborhood; and/or are not able to obtain conventional mortgage financing
- Applicant must be [sic] willing to invest in 100 hours of sweat equity labor in helping to house renovate your and the houses of others
- Applicant must agree to attend mandatory Homeownership educational workshops
- Applicant is committed to living in a drug-free and crime-free community
- Applicant is aware that all members of your household who are 18 years or older must not be listed on the sex offender registry and each individual must pass a national criminal background check
- Applicant must show proof that your family's income falls within the income guideline. You understand that income must be counted for all family members over 18 years of age
- Applicant will pay off all judgments within 90 days of application
- Applicant will set up payment plans to pay off all collections
- Applicant must understand that if you have ever filed bankruptcy, it has been 5 years since the discharge of a Chapter 7 bankruptcy or at least 3 years since the discharge of a Chapter 13 bankruptcy, and
- Applicant understands that you will be required to pay a cash down-payment of \$1,000, to pay \$500 prior to closing to cover your first year's homeowners insurance and closing costs, and to make a monthly mortgage payment that will not exceed 29% of your gross income.

You also stated at this time that you follow HUD's Area Median Income (AMI) guidelines to establish eligibility using relationship of family size and income limits. You submitted a sample of the HUD guidelines. You said you will reject a buyer if they do not fall within HUD's AMI guidelines.

You initially indicated each applicant is required to have a 3.5% down payment. When asked for clarification, you indicated individuals for whom you provide housing must earn no more than 120% of the very low income levels using federal guidelines. Applicants must have gross income of at least \$25,000 but less than \$40,000 and a 3.5% down payment. You then indicated an applicant must have a \$1000 down payment and fall within HUD's AMI guidelines. Finally, you stated that a down payment of \$1000 minimum or 3.5% of the sales price, whichever is greater, is required. In addition you submitted the HUD guidelines previously submitted.

You will use P to obtain the properties you will renovate. Q will be a project manager and will oversee the projects during the construction phase, compensated at the rate of \$20/hour. Although you indicated you would

entertain bids for your construction projects, with criteria you use to choose including “experience, reputation and cost,” you said there was no actual bid process for selecting Q because you don’t have any projects. “The industry standard for project management on construction is a 30% mark up. Q has agreed to charge only \$20 per hour for project construction management.”

You will use P to sell the properties you renovate. You will advertise your properties for sale through the Multiple Listing Service (MLS), and P will receive a standard fee of 6% of the sales price as a commission. Prices of the homes you sell will be between \$50,000 and \$125,000; determined by the average of three comparable properties within a one mile range of the subject property that is purchased.

You said you would consider other listing/brokerage companies if the homes can be listed/sold for 6-8% commission. P was selected as real estate broker used for home sales because it can provide the lowest real estate commission at 6% compared to other real estate companies that charge at least 10%.

We asked for documentation on the process used to select Q and P to perform services. As you have not done an actual project at this time, there was no process for selecting Q or P to perform services. You also submitted no other documentation on the process of selecting other contractors to perform any of your needed services.

Your initial budgets included only salaries, occupancy and professional fee expenses. You also showed only donations as projected revenue, with no income from housing sales. When questioned on the seemingly low amounts projected, and the lack of expenses related to your direct activities, you stated “we will obtain renovation bank loans to renovate and acquire the property. The current budget is based on proceeds received after renovation loans and all other expenses associated paid in full.”

We attempted to further clarify your projected revenue and expenses. You then provided a sample budget for a project. This included purchase price, rehab costs, and holding and financing costs. In addition the budget included a “flip profit” line, which was about 11% of the sales price. The projected purchase price and rehabilitation costs alone were around seven times more than the projected amount previously given.

Law

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable, educational, and scientific purposes.

Treasury Regulation Section 1.501(c)(3)-1(a)(1) states that, in order to be exempt as an organization described in Section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Treasury Regulation Section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as “operated exclusively” for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in Section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Treasury Regulation Section 1.501 (c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

Treasury Regulation Section 1.501(c)(3)-1(d)(1)(ii) requires that the applicant organization must show that it serves a public rather than a private interest and, specifically, that it is not organized or operated for the benefit of private interests, such as designated individuals, the creator or his family, shareholders, of the organization, or persons controlled, directly or indirectly, by such private interests.

Treasury Regulation Section 1.501-1(d)(2) defines the word “charitable” as used in Section 501(c)(3) of the Code as including the relief of the poor and distressed. The term charitable also includes the erection or maintenance of public buildings, monuments or works, lessening the burdens of government, and the promotion of social welfare by combatting community deterioration.

Revenue Ruling 70-585 1970-2 CB 115: Nonprofit housing organizations created to aid low and moderate income families by lessening neighborhood tensions, eliminating prejudice and discrimination, and combating community deterioration may qualify for exemption under section 501(c)(3) of the Code.

Revenue Procedure 96-32 (I.R.B. 1996-20) sets forth a safe harbor under which organizations that provide low-income housing will be considered charitable because they relieve the poor and distressed as described in Reg. S1.501(c)(3)-1(d)(2). The safe harbor contained in this revenue procedure identifies those low-income housing organizations that will, with certainty, be considered to relieve the poor and distressed. Low-income housing organizations that fall outside the safe harbor may still be considered organizations that offer relief to the poor and distressed based on all the surrounding facts and circumstances.

Revenue Procedure 2015-9: A favorable determination letter or ruling will be issued to an organization only if its application and supporting documents establish that it meets the particular requirements of the section under which exemption from federal income tax is claimed. The applicant is responsible for the accuracy of any factual representations contained in the application. The failure to disclose a material fact or misrepresentation of a material fact on the application may adversely affect the reliance that would otherwise be obtained through issuance by the Service of a favorable determination letter or ruling. A mere restatement of exempt purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. Where the organization cannot demonstrate to the satisfaction of the Service that it qualifies for exemption the Service will generally issue a proposed adverse determination letter or ruling.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U. S. 279 (1945), the Supreme Court of the United States interpreted the requirement in Section 501(c)(3) that an organization be “operated exclusively” by indicating that an organization must be devoted to exempt purposes exclusively. This plainly means that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number and importance of truly exempt purposes.

In Easter House v. United States, 12 Cl. Ct. 476, 486 (Cl. Ct. 1987), aff’d 846 F.2d 78 (Fed. Cir 1988), the court found that adoption services were the primary activity of the organization. In deciding that the organization conducted adoption services for a business purpose rather for a charitable purpose, the court considered the manner in which the organization operated. The record established a number of factors that characterized a commercial activity and which were evident in the operations of Easter House also. The court determined that the organization competed with other commercial organizations providing similar services, fees were the only source of revenue, it accumulated very substantial profits because it set its fees in order to

generate a profit, the accumulated capital was substantially greater than the amounts spent on charitable and educational activity, and the organization did not solicit and did not plan to solicit contributions.

In P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), an organization operated bingo at a bar (a for-profit enterprise) for purposes of raising money for scholarships. The board of directors included the bar's owners and accountant, and two other persons. The court reasoned that, because the bar owners controlled the organization and appointed its directors, the organization's fundraising activities could be used to the advantage of the bar owners, and thus, provide them with a maximum private benefit. The organization claimed that it was independent because there was a separate accounting and that no payments were going to the bar. The court maintained that the organization's and the bar's activities were so interrelated as to be "functionally inseparable." A separate accounting did not change that fact. Thus, the organization did not operate exclusively for exempt purposes, but rather benefited private interests – the bar owners. Exemption was properly denied.

Application of law

You have not demonstrated that you are organized and operated exclusively for charitable, educational, or other purposes and that no part of your net earnings inure to the benefit of private shareholders or individuals as required by section 501(c)(3) of the Internal Revenue Code. (Regulation Section 1.501(c)(3)-1(a)(1)). You also fail to meet the operational test in that you are operated primarily for the purpose of carrying on a trade or business of buying, rehabilitating and selling or leasing real property, which consists of more than an insubstantial portion of your activities. (Regulation Section 1.501(c)(3)-1(c)(1)) Despite citing educational programs, you provide little to no documentation on these programs, including when and where they are conducted, how often, what you cover in these programs, materials used, or who teaches these programs. Further, you have not established that your operations serve public rather than private interests. (Regulation Section 1.501(c)(3)-1(d)(1)(ii))

You are not described in Section 1.501(c)(3)-1(c)(1) because more than an insubstantial part of your activities are devoted to non-exempt purposes. Your proposed activity of purchasing, renovating and selling homes to low income individuals, of itself, is not a charitable activity within the meaning of Section 1.501(c)(3)-1(d)(2). You have not demonstrated that the services you provide or fees charged for those services are offered exclusively for exempt purposes.

Treasury Regulation Section 1.501(c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. By using the for-profit businesses of your governing body members to conduct all of your activities, you are operating for the private interests of these businesses, and subsequently, these individuals, rather than a public interest. In contravention to your Bylaws, 75% of the members of your governing body are interested parties and the two entities you have selected to conduct business, P and Q, were not selected without conflict of interest. Your activities directly advance the interests of P and Q and designated board members will receive financial benefits as a result. Therefore, you do not qualify for exemption under Section 501(c)(3) because your operations result in inurement to the board members that own P and Q.

Housing, although not of itself a charitable purpose, may qualify for exemption under 501(c)(3) if conducted in a charitable manner. (Revenue Ruling 70-585) While you have indicated your intent to serve a low income class, you have been unable to substantiate how you will meet the guidelines established through Revenue Ruling 70-585 as well as any safe harbor guidelines established through Revenue Procedure 96-32. Numerous inconsistencies have been documented through your application process that you have not fully clarified despite

multiple attempts. Instead, you appear to be operating a house renovation business ordinarily carried on for-profit. You make use of a related real estate company to select and sell homes (P), and a related construction company (Q) to renovate these homes before sales. Rather than first identifying potential low income buyers, you advertise homes for sale through the MLS. Your project budget, which included a “flip profit”, indicates you will be dependent on funds relative to profit generated through sales rather than charitable contributions. The sale of homes on a regular basis, in a manner typically carried on by a for-profit organizations, denotes the carrying on of a trade or business, similar to the organization in Easter House, which did not qualify for exemption.

You use P not only for buying and selling services, but also as your physical location. One of your directors is an owner of P. P is listed as your registered agent. You conduct activities similar to and along with those of P and Q – real estate purchase, development and sales. You pay P and Q for services and P handles home sale transactions. As a result, it is difficult to distinguish your operations from those of P. In P.L.L. Scholarship Fund, an organization operated bingo at a bar (a for-profit enterprise) for purposes of raising money for scholarships. The organization’s and the bar’s activities were so interrelated as to be “functionally inseparable.” The organization did not operate exclusively for exempt purposes, but rather benefited private interests – the bar owners. Exemption was properly denied. Here, you appear functionally inseparable from P and, to an extent, Q. Your activities are structured to directly benefit the owners of P and Q, and you do not operate exclusively for exempt purposes but rather for private interests and do not qualify under 501(c)(3).

You are similar to the organization in Better Business Bureau in which the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes. Your activity of rehabilitating houses and selling them is an activity that is primarily carried on for the purpose of conducting a commercial business.

You have been unable to substantiate that your housing programs are exclusively serving charitable purposes in terms of serving a charitable class. On multiple occasions information has been requested to document how you are meeting the guidelines of Revenue Procedure 96-32, as well as Revenue Ruling 70-585, regarding low income housing activities. You submitted incomplete and contradictory facts on each response. Additionally, contradictory statements regarding your activities have been submitted throughout the application process which has not allowed us to fully evaluate the charitable aspects of your programs or to clearly distinguish the private interests of members of your organization including your governing body. Per Revenue Procedure 2015-9, where an organization cannot demonstrate to the satisfaction of the Service that it qualifies for exemption the Service will generally issue a proposed adverse determination letter or ruling.

Conclusion

Based on the information provided, you do not qualify for exemption under Section 501(c)(3) of the Code. You are not operated exclusively for charitable purposes within the meaning of Section 501(c)(3), because you are serving private interests and conduct non-charitable activities.

If you don’t agree

You have a right to file a protest if you don’t agree with our proposed adverse determination. To do so, you must send a statement to us within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number

- A copy of this letter highlighting the findings you disagree with
- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

Under penalties of perjury, I declare that I examined this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

For authorized representatives:

Under penalties of perjury, I declare that I prepared this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't provided a basis for reconsideration, we'll forward your case to the Office of Appeals and notify you. You can find more information about the role of the Appeals Office in Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

Where to send your protest

Please send your protest statement, Form 2848, if needed, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at www.irs.gov/formspubs. If you have questions, you can contact the person listed at the top of this letter.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosure:
Publication 892